

Members

Sen. Joseph Harrison, Chair
Sen. Thomas Weatherwax
Sen. Allie Craycraft
Sen. Larry Lutz
Rep. Thomas Kromkowski
Rep. Ron Liggett
Rep. Lawrence Buell
Rep. Richard Mangus
Steve Meno
Claude Davis
William Gettings, Jr
Connie Lux



PENSION MANAGEMENT OVERSIGHT COMMISSION

Legislative Services Agency
200 West Washington Street, Suite 301
Indianapolis, Indiana 46204-2789
Tel: (317) 232-9588 Fax: (317) 232-2554

LSA Staff:

Jim Sperlik, Fiscal Analyst for the Commission
Ed Gohmann, Attorney for the Commission

Authority: IC 2-5-12-1

MEETING MINUTES¹

Meeting Date: September 15, 1999
Meeting Time: 10:00 A.M.
Meeting Place: State House, 200 W. Washington St.,
Room 156-D
Meeting City: Indianapolis, Indiana
Meeting Number: 1

Members Present: Sen. Joseph Harrison, Chair; Sen. Allie Craycraft; Sen. Larry Lutz;
Rep. Thomas Kromkowski; Rep. Ron Liggett; Rep. Richard Mangus;
William Gettings, Jr; .

Members Absent: Sen. Thomas Weatherwax; Rep. Lawrence Buell; Steve Meno;
Claude Davis; Connie Lux.

1) Taxation of Federal Retirees

The Chair of the Pension Management Oversight Commission (PMOC), Sen. Harrison, called the first meeting to order at 10:15 A.M. Sen. Harrison then introduced the PMOC members and the staff. He next called upon Ms. Mary Beth Braitman of the law firm of Ice Miller Donadio & Ryan, outside counsel for the Public Employees Retirement Fund (PERF) and the Teachers' Retirement Fund (TRF). Prior to Ms. Braitman's comments on the topic of taxation of federal retirees, the staff distributed: (1) a chart prepared by the National Conference of State Legislatures (NCSL) which showed how states tax various types of retirement income; (2) a chart prepared by Ms. Braitman which compared how states tax state retirement benefits and federal retirement benefits; (3) a memorandum prepared by Ms. Diane Powers of the Office of Fiscal and Management Analysis of the Legislative Services Agency, which estimated the amount of income tax revenue generated by various sources of pension income.

Ms. Braitman told the PMOC that Indiana public employee benefits are fully taxable. She explained that federal civil service employees are allowed a \$2,000 deduction for those who are at least 62 years of age, but that this deduction is reduced by the Social Security and Railroad

¹Exhibits and other materials referenced in these minutes can be inspected and copied in the Legislative Information Center in Room 230 of the State House in Indianapolis, Indiana. Requests for copies may be mailed to the Legislative Information Center, Legislative Services Agency, 200 West Washington Street, Indianapolis, IN 46204-2789. A fee of \$0.15 per page and mailing costs will be charged for copies. These minutes are also available on the Internet at the General Assembly homepage. The URL address of the General Assembly homepage is <http://www.ai.org/legislative/>. No fee is charged for viewing, downloading, or printing minutes from the Internet.

retirement benefits received. Ms. Braitman further noted that a survey of the fifty states revealed that 20 states either have no income tax or provide a full exemption to state and federal retirees, eight states fully tax both state and federal retirees, while the remaining twenty-two states provide a range of exemptions. Ms. Braitman went on to say that only four states differ in their treatment of state and federal retirees. These states are Kentucky, West Virginia, North Dakota, and Indiana. The other forty-six states treat the state and federal retirees the same.

The Chair next recognized Mr. Paul Severance of the United Senior Action. Mr. Severance told the PMOC that there is a fundamental lack of fairness in the taxation of retiree income. He said that he was asking for fairness and that all retirees, whether under Social Security or another system, should be treated equally.

Sen. Harrison called upon Mr. Frank Tester, Area 2 Vice-President of the Indiana Federation of the National Association of Retired Federal Employees (NARFE). Mr. Tester distributed his prepared text. He said that there is great discrimination in the income taxation between various groups of retired persons in Indiana. He suggested the following as possible ways to equalize the treatment:

- a) eliminate the income tax deduction for all retired senior citizens in Indiana including those receiving Social Security.
- b) reduce the income tax deductions granted to those retired under Social Security in Indiana to that which is granted those who are retired under other systems in Indiana.
- c) add the present deductions received by Civil Service, military, and Social Security retirees and divide the total among all for equalized deduction.
- d) grant the same income tax deductions to all retired citizens in Indiana as are now granted those retired under Social Security.

Sen. Harrison next recognized Mr. Joseph H. Ziegler, Area 6 Vice-President of NARFE. In prepared text for the PMOC, Mr. Ziegler said that he was appearing before the PMOC to support the proposition that all retired persons in Indiana should be treated equally under income tax laws, regardless of where they were employed during their working years.

Mr. Claude Ferguson, Legislative Chairman of NARFE, was then recognized by the Chair. In his prepared testimony Mr. Ferguson told the PMOC that he chose to live in Indiana after he had retired, but feels that he is treated as a second class citizen in the way his retirement income is taxed. He said that year after year he must pay more income tax than his neighbors who chose to work under Social Security in private employment.

The Chair next called upon Ms. Grace Wolfe. Ms. Wolfe told the PMOC that she is a civil service survivor annuitant. She said that her husband had spent 30 years working with the U.S. Department of Defense before his retirement. Ms. Wolfe told the PMOC that she was testifying to support equal treatment under the Indiana income tax laws for all of the retired citizens in Indiana.

Ms. Phillis Hurd, President of Chapter 151, NARFE, next addressed the PMOC. In her prepared text, Ms. Hurd told the PMOC that she retired after 33 years of service in a variety of government agencies. She said that she was testifying because she strongly supports the proposal that the federal government retirees be treated equally under the income tax statutes of Indiana. She further commented that the action NARFE proposes would bring Indiana into line with other states, while establishing equal treatment for those citizens retired under the Social Security System and the United States Civil Service System.

Sen. Harrison next called upon Lt. Col. Joseph B. Duray, U.S. Army (Retired). In his prepared

text, Mr. Duray, speaking as a member of the Retired Officers Association and the Military/Veterans Coalition of Indiana, said that he supports the proposed “Equity In Pensions” treatment of federal retirement pay.

Next to address the PMOC was Mr. Charles Caton of The Retired Enlisted Association (TREA). In prepared testimony, Mr. Caton told the PMOC that he and his organization support the proposition that all retired citizens of Indiana should receive the same tax deductions, regardless of how or where they were employed during their working years.

Mr. Allen Lauer, a retired employee from the post office in Ft. Wayne and a member of NARFE, told the PMOC, in prepared testimony, that he was appearing in support of the proposition that all retired citizens in Indiana should receive the same income tax deduction regardless of the form of their employment during their working years. He went on to say that retired letter carriers, their families, and survivors are presently treated very unfairly as senior citizens of Indiana. In response to a PMOC question, Mr. Lauer said that the average annual pension for a letter carrier with forty years of experience is approximately \$26,000.

Mr. Douglas Brown, Legislative Director for the Indiana Postal Workers Union, next addressed the PMOC. Mr. Brown stated that he supports legislation that will treat all retired citizens of Indiana equally on income tax deductions, regardless of where they were employed.

Mr. Martin Hindman of NARFE told the PMOC that he supports fairness in the taxation of federal retirees. Mr. Richard Waite of NARFE said that civil service employees contribute 7% of their salary, while Social Security recipients contribute 6.2%. Ms. Lynn Conrad of the Bloomington chapter of NARFE told the PMOC that she strongly endorses tax equity for civil service retirees. Ms. Esther Meek said that she is concerned about the lack of a tax deduction for civil service annuitant survivors. Former state Representative Don Dean told the PMOC that he supports fairness in the treatment of civil service retirees.

2) PERF/TRF Legislation

Sen. Harrison called upon Ms. Mary Beth Braitman, outside counsel for PERF and TRF. Ms. Braitman noted that she has attended the PMOC meetings over the last ten years and that there have been consistent themes to which the PMOC returns. The first, she said, is that of modernization of the pension plans. According to Ms. Braitman, some of the best examples include the passage of the equity referendum in 1996; the restructuring of the annuity savings accounts to include meaningful and dynamic choices; and the on-going diversification of the funds’ portfolios and the use of the finest financial advisors and investment managers in the country. She told the PMOC that one might characterize these changes as moving from the 19th century to the 21st century.

Continuing, Ms. Braitman said that the second theme is adequate and actuarially sound funding of the pension commitments. She said that the PMOC has worked for the last decade to make massive improvement in the funds’ actuarial soundness. That process has included restructuring to have a new currently funded TRF plan, as well as devoting massive resources to improving the funding of the old TRF plan. It also has included major changes in the funding for police and firefighter pensions, providing hundreds of millions of dollars of city and town relief, and significantly closing the local unit shortfall. Ms. Braitman also told the PMOC that PERF is now fully funded to the current day, with employer contribution rates dropping correspondingly to cover only the new accruals.

The third theme, according to Ms. Braitman, is member services and benefits. She said that there are numerous examples of the PMOC’s activity in this regard throughout the last decade. She said that the PMOC members have sponsored legislation improving police and firefighter

survivor benefits; adding the Rule of 85 early retirement for PERF and TRF; adding member investment direction preretirement and post retirement; and reducing the retirement age for public safety officers.

Ms. Braitman told the PMOC that the concept she wanted to introduce is grounded in all three themes and is a natural continuation of the PMOC's work in those areas. She said that it entails redefining the funds as separate bodies corporate and politic, in addition to their existing trust fund status. Ms. Braitman said that this concept would complete the modernization of the funds, it would provide a workable funding solution for their operational expenses, and it would allow measurable improvements in member service and communications.

Ms. Braitman said that this concept is not a unique or unusual one. There are numerous examples of separate bodies corporate and politic in Indiana: the Indiana Development Finance Authority, the State Student Assistance Commission, the State Office Building Commission, the Lottery Commission. She also said that there are numerous examples of this concept in other Midwest state pension systems and that nine similar approaches exist around Indiana.

Ms. Braitman stated that a separate body structure would not change the trustees' fiduciary duties and their state and federal legal requirements to use trust assets for the exclusive benefit of plan members and to administer the funds as prudent experts; it would also not change the funds' relationships to the Auditor, the Treasurer, the Governor, or the State Board of Accounts. She explained that it would also not change the source of operational expenses. They are currently paid from the funds' own assets, not the state's general fund. The new structure would change the funds' budget process and the trustees would create the fund budgets based on their staffing plans. The budgets would be reported completely and fully to PMOC. The trustees currently report their investment performance to PMOC.

Ms. Braitman stated that the proposed new structure also would change the funds' responsiveness time to changing markets and conditions and to members' requests. Ms. Braitman said that the structure would allow the trustees to secure adequate staff and resources to meet member expectations, respond to changing economic markets, products and conditions, and fulfil their fiduciary responsibilities.

Ms. Braitman closed her presentation by paraphrasing from the commentary for the new Uniform Act for the Management of Public Employee Retirement System, stating that public pensions trustees are different from other state bodies because they are subject to an extensive and stringent set of fiduciary obligations under both state and federal law and that a level of independence is, therefore, required to permit them to perform those duties while complying with their fiduciary responsibilities.

Sen. Harrison next called upon Mr. William Butler, Director of PERF. Mr. Butler told the PMOC that the PERF Board of Trustees takes its fiduciary responsibilities seriously. He said that they are responsible for \$10 billion in assets. Mr. Butler also stated that the PERF Board supports the proposal to establish the funds as separate bodies corporate and politic.

Mr. William Christopher, Director of TRF, was recognized by Sen. Harrison. Mr. Christopher told the PMOC that modernizing the administrative process would allow TRF to respond quickly and effectively, and that he supported the proposal.

The Chair then called upon Mr. Tom Miller, President of the Professional Fire Fighters Union of Indiana. Mr. Miller said that Indiana has made great strides over the last decade and that this proposal would make Indiana more like other states.

Mr. Leo Blackwell of the Indiana Fraternal Order of Police (FOP) told the PMOC that the FOP

supports wholeheartedly the new proposal.

3) Prosecuting Attorneys Retirement Fund (PARF) Issues

Ms. Deborah Daniels, representing the Prosecuting Attorneys Council, was recognized by Sen. Harrison. Ms. Daniels told the PMOC that the Prosecuting Attorneys are requesting changes to the PARF statutes. Ms. Daniels distributed a memorandum entitled Requests of Prosecuting Attorneys for Changes to the PARF, specifying these changes. Ms. Daniels introduced Mr. Richard A. Maughmer, Prosecuting Attorney from Cass County. In his presentation, Mr. Maughmer told the PMOC that the proposal would do the following:

- a) provide for the prorating of benefits for partial years of service;
- b) eliminate the requirement for members to contribute after 22 years of service;
- c) increase the percentages used in computing disability benefits to match the Judges' Retirement System provisions;
- d) eliminate the requirement of five years of service for disability benefits;
- e) reduce the number of years required to vest from ten to 8 years;
- f) reduce the reduction factors for retirement age 65 (from 0.25% to .01% for each month that participant's age at retirement precedes 65th birthday;
- g) increase percentages used in computing retirement benefits to match the Judges' Retirement System;
- h) revise definition of disability to an inability to serve as a prosecuting attorney.

The Chair next recognized Mr. Steve Johnson, Prosecuting Attorney from Grant County. Mr. Johnson told the PMOC that there are two types of prosecutors — one runs strictly because of the job; the other its dedicated to the profession and the position.

In response to questions from the Chair, Mr. Maughmer told the PMOC that there are approximately 30 part-time prosecutors and that the salary of a full-time prosecutor is the same as that of a judge, \$90,000 per year. In addition, Mr. Maughmer told the PMOC that the increase in annual funding for this proposal is estimated at \$738,000 (parts a through h above) and that without this funding the increase in unfunded liabilities would be \$4,120,000.

4) Internal Revenue Service Ruling

Ms. Braitman was recognized by Sen. Harrison. Ms. Braitman brought to the PMOC an issue dealing with the taxation of line-of-duty death and disability benefits. Ms. Braitman told the PMOC that the police and firefighter funds have submitted a request for a private letter ruling to the Internal Revenue Service (IRS) regarding this issue. The IRS has suggested in negotiations that if certain structural, not substantive, changes are made to the police and firefighter funds, the IRS would rule death benefits to be non-taxable.

5) Other Business

Rep. Tom Kromkowski was recognized by Sen. Harrison. Rep. Kromkowski told the PMOC that a fiscal note for military service credit for teachers on HB 1345 from the 1999 Legislative Session seemed high to him and he would like to explore this issue during the Commission's deliberations this year. Mr. Steve Moberly, Executive Director the Indiana Retired Teachers Association was recognized by the Chair, and he told the PMOC that he has contacted the actuaries for the TRF, but has not heard back from them on how the costs for the military service credit were calculated.

Sen. Harrison set the next meeting for Wednesday, October 13th at 10:00 A.M. With no further business, the Chair adjourned the meeting at 11:50 A.M.